

MULTIMEDIA



UNIVERSITY

STUDENT ID NO

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MULTIMEDIA UNIVERSITY

FINAL EXAMINATION

TRIMESTER 2, 2019/2020

BAW 4614 – ADVANCED FINANCIAL ACCOUNTING & REPORTING

(All Section / Groups)

2 MARCH 2020
9.00 a.m – 12.00 p.m.
(3 Hours)

INSTRUCTIONS TO STUDENT

1. This question paper consists of 9 pages with 4 questions only. Answer all questions. The distribution of marks is shown at the end of each question.
2. Please write your answers in the answer booklet provided.
3. Students are required to apply IFRS framework.

QUESTION 1

Whitey Ltd is a manufacturing company which sells online to both trade and retail customers. It also operates a recycling business. You, an ICAEW Chartered Accountant, was recently employed in the finance department at Whitey Ltd. Your first role is to assist the finance director in the preparation of the financial statements for the year ended 31 December 2019.

The following balances have been extracted from the nominal ledger of Whitey Ltd at 31 December 2019.

	Notes	£	£
Land and buildings	(1), (2)	1,155,500	
Plant and equipment	(2)	103,200	
Inventories at 31 December 2018		63,400	
Trade and other receivables		86,400	
Cash at bank		14,800	
Trade and other payables	(3)		99,200
Ordinary share capital (£1 shares)			500,000
Retained earnings at 31 December 2018			97,700
5% £1 convertible redeemable preference shares	(4)		100,000
Sales			3,068,000
Purchases		1,664,200	
Administrative expenses		512,800	
Operating costs		324,600	
Other income	(5)		60,000
		3,924,900	3,924,900

Notes:

- On 1 January 2019 Whitey Ltd had purchased a recycling plant for £240,000 in order to process hazardous waste generated as a by-product of its other operation. The plant has an estimated useful life of 10 years from the date of acquisition, after which it is expected to be superseded by new technology. It was a condition of the purchase that Whitey Ltd must dismantle the plant and restore the land at the end of the 10 years. The cost of dismantling and restoration is estimated to be £80,000 at the purchase date. The only accounting entries made by Whitey Ltd were to debit land and buildings and credit cash with the £240,000 purchase cost.

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2. The following information relates to Whitey Ltd's property, plant and equipment.

	Freehold land and buildings	Plant and machinery
	£	£
Cost (land £500,000)	1,640,000	150,000
Accumulated depreciation at 31 December 2018	484,500	46,800

Depreciation for the year ended 31 December 2019 has not been charged. Unless otherwise indicated, buildings are depreciated at 2.5% pa on straight-line basis and plant and equipment is depreciated on reducing balance basis at a rate of 12.5%. Depreciation is recognised in cost of sales.

3. Whitey Ltd had purchased 600 units of product D from an overseas supplier on 1 November 2019 for €15,000. As at year end, 450 units of product D were still held in the warehouse. These inventories were not included in the inventory count as they had been stored in a different area. The invoice was unpaid at 31 December 2019 and was included in trade payables at the exchange rate on the date of purchase.

The spot exchange rates were as follows:

1 November 2019	€1: £0.56
31 December 2019	€1: £0.70

4. On 1 January 2019 Whitey Ltd issued 100,000 5% convertible redeemable preference shares at par (nominal value £1 each). The preference shares are redeemable at par for cash on 31 December 2021, or are convertible into 20,000 new £1 ordinary shares at that date. On 31 December 2019 the preference dividend due had not been paid and no accounting entries made. An interest rate on similar redeemable preference shares without the conversion options is 8% pa. The only accounting entries made at 31 December 2019 were to recognise the £100,000 cash received as an equity.
5. A government grant of £60,000 was received on 1 October 2019 in respect of starting a training course for school leavers. A condition of the grant is that the training course must be in existence for 2 years after the grant was received. This is the full amount of the grant and it has been debited to cash and credited to other income. The training course started on 1 October 2019 and is expected to run for 24 months. The training has been an overriding success and Whitey Ltd's directors believe that the training course will continue to exist for the foreseeable future.
6. Inventories were counted and valued at 31 December 2019 at £43,000. Shortly after the year end, you discovered that finished goods inventories held by the division have been valued at their cost. However, because of the imminent sale, Whitey Ltd expects to have to discount every product line by 30% and to incur selling costs of £1 per unit. Costs and selling prices are as follows:

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Product reference number	Number of units in inventory	Valued at cost	Current selling price per unit
		£	£
A	100	550	8.00
B	150	1,050	12.00
C	500	2,250	3.00
	750	3,850	

7. The income tax liability for the year ended 31 December 2019 has been estimated at £108,000.

An appropriate discount rate is 6% pa.

Requirement

Prepare a statement of profit or loss for Whitey Ltd for the year ended 31 December 2019 and a statement of financial position as at that date in a form suitable for publication.

(27 marks)

(Total: 27 marks)

QUESTION 2

You are an ICAEW Chartered Accountant on secondment to Purple Ltd., helping to prepare financial statements for the year ended 31 December 2019. The secondment is for six months whilst the finance director, who is also an ICAEW Chartered Accountant, is on maternity leave. The managing director has requested you to check and redraft the following disclosure notes as he is concerned that it may contain errors. The disclosure notes were drafted by the finance director before her maternity leave. All the directors of Purple Ltd receive a bonus linked to the profit for the year.

Since you joined Purple Ltd, you have heard rumours that the finance director has a dominant personality. Your predecessor left because he disagreed with the finance director over the accounting treatment of some issues.

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	Properties £	Plant and machinery £
Cost/valuation		
At 1 January 2019	2,501,200	1,053,600
Additions	-	151,200
Revaluation	200,000	-
At 31 December 2019	<u>2,701,200</u>	<u>1,204,800</u>
Accumulated depreciation		
At 1 January 2019	691,200	632,000
Charge for the year	50,200	120,480
At 31 December 2019	<u>741,400</u>	<u>752,480</u>
Carrying amount		
At 31 December 2019	1,959,800	452,320
At 31 December 2018	1,810,000	421,600

Notes

1. Purple Ltd entered into a three-year lease for machinery on 1 January 2019 with a fair value of £124,000. An initial lease payment of £32,000 was made on 1 January 2019. Three further annual instalments of £32,000 each are due in arrears, the first of which was paid on 31 December 2019. The machine has useful life of four years. The present value of the minimum lease payments at 1 January 2019, based on an annual interest rate of 5% is £119,142. The finance director debited the actual lease payments made in the year to plant and machinery, and they are included in additions in the table above.
2. The only other figure included in additions to plant and machinery was a machine purchased on 1 September 2019.
3. The above table has not recognised the following transactions:
 - On 1 January 2019 the directors decided to change the depreciation method for plant and machinery from a straight-line basis over a 10-year useful life to 20% reducing balance, as this is considered to be a better reflection of the consumption of economic benefits.
 - A machine was sold for scrap on 1 January 2019. The machine had cost £30,000 on 1 January 2012 and was sold for cash of £1,600. The finance director credited the cash received to revenue.

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4. Properties consist of land and building. Properties are carried under the revaluation model and plant and machinery is carried under the cost model. The depreciation charges in the table above were calculated using the depreciation methods in place at 31 December 2018.
5. The revaluation during the year related to a piece of land which had previously been valued in 2017 at £700,000. The land had cost £665,200 in 2015. The land was revalued for the first time in 2017 when the excess of valuation over carrying was credited to the revaluation surplus.

During the year, the revaluation was based on a report commissioned by the finance director from Blue Consultancy, a firm of chartered surveyors wholly owned by the finance director's brother. The report showed the value of land at £900,000 on 31 December 2019. Blue Consultancy invoiced Purple Ltd £2,000 for the report in January 2020 and Purple Bhd accrued for this invoice at 31 December 2019. The finance director recognized the revaluation increase as income in the statement of profit or loss for the year ended 31 December 2019 on the grounds that in early 2020 the directors decided to sell this property.

The land was sold in February 2020 for only £651,000, following the discovery in early January 2020 that the land had been contaminated in the previous year and needed remedial work to restore it to a usable condition. The land did not meet the definition of a held for sale asset at 31 December 2019.

Required:

- a. Present a proposal to the directors on how the matters described in Note 5 above should have been dealt with in Purple Ltd's financial statements for the year ended 31 December 2019. (8 marks)
- b. Prepare the second draft of the disclosure note showing the movements on property, plant and equipment for inclusion in Purple Ltd's financial statements for the year ended 31 December 2019. (8 marks)
- c. The concept of substance over form is implied within faithful representation, one of the qualitative characteristics of the IASB's *Conceptual Framework*. Explain the concept of substance over form and how it should be applied to the transactions described in Note 1. (4 marks)
- d. Discuss the ethical issues arising for you and the finance director from the above scenario and the actions that you should take. (5 marks)

(Total: 25 marks)

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QUESTION 3

You are the assistant accountant at Begania Ltd and are helping to prepare the company's individual and consolidated financial statements for the year ended 30 September 2019. There are a number of outstanding issues which need to be resolved.

An extract from Begania Ltd 's draft financial statements for the year ended 30 September 2019 shows:

Statement of financial position at 30 September 2019 (extract)		
	2019	2018
	£	£
Non-current assets		
Property, plant and equipment	863,600	752,600
Non-current liabilities		
Lease liabilities	75,516	-
Current liabilities		
Lease liabilities	22,784	-

The following additional information is available.

1. The draft reconciliation of profit before tax to cash generated from operations shows 'Cash generated from operations' as £374,640.
2. On 1 October 2018, Begania Ltd entered into a lease for a new machine with a cash price of £120,000, which is its fair value. The terms of the agreement require five annual payments of £27,700, commencing on 30 September.
3. During the year, fixtures and fittings were acquired for cash. The correctly calculated depreciation charge for the year ended 30 September 2019 was £83,000. A machine with a carrying amount of £27,400 was disposed of during the period with a loss of £8,700 being recognised on its disposal. Equipment with a carrying amount of £4,800 was scrapped.
4. Begania Ltd sold all of its 85% holding in Gaania Ltd's 350,000 £1 ordinary shares on 1 March 2019, for cash consideration of £560,000.
5. Begania Ltd paid £450,000 on 1 October 2014 for the 85% shares in Gaania Ltd when the retained earnings of Gaania Ltd were £87,600. The fair value of the assets, liabilities and contingent liabilities of Gaania Ltd on that date were equal to their carrying amounts. Goodwill was calculated using the proportionate method, although £30,000 of this amount had been written off last year.
6. On 30 September 2019, Gaania Ltd had retained earnings of £292,000, including a profit for the year ended 30 September 2019 of £144,000. There is no change in the ordinary shares since incorporation.

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Requirements

- a. Prepare an extract from Begania Ltd statement of cash flows for the year ended 30 September 2019, showing:
- a revised figure for 'Cash generated from operations'.
 - cash flows from investing activities.
 - cash flows from financing activities.
- (7 marks)
- b. Explain how the profit or loss from discontinued operations should have been calculated in accordance with IFRS 5, *Non-current Assets Held for Sale and Discontinued Operations*, and calculate the relevant figure. (7 marks)
- c. Describe any differences between IFRS and UK GAAP in respect of the financial reporting treatment of the disposal of Gaania Ltd. (4 marks)

(Total 18 marks)

QUESTION 4

Titan Plc has investments in two companies, Iron Ltd and Echo Ltd, and recognises goodwill and non-controlling interest using the proportionate method.

The draft, summarised statements of financial position of the three companies at 31 December 2018 are shown below:

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	Titan Plc £	Iron Ltd £	Echo Ltd £
Assets			
Non-current assets			
Land	3,200,000	500,000	
Other tangible non-current assets	1,140,000	1,696,000	591,900
Investments	1,700,000	-	-
Goodwill	-	-	30,000
	<u>6,040,000</u>	<u>2,196,000</u>	<u>621,900</u>
Current Assets			
Inventories	200,000	54,000	180,100
Trade and other receivables	281,500	334,800	186,000
Cash and cash equivalents	18,500	12,700	2,000
	<u>500,000</u>	<u>401,500</u>	<u>368,100</u>
Total assets	<u>6,540,000</u>	<u>2,597,500</u>	<u>990,000</u>
Equity and Liabilities			
Equity			
Ordinary share capital	2,750,000	950,000	360,000
Retained earnings	3,239,400	1,200,000	176,000
	<u>5,989,400</u>	<u>2,150,000</u>	<u>536,000</u>
Current liabilities			
Trade and other payables	400,600	220,800	442,400
Taxation	150,000	226,700	11,600
	<u>550,600</u>	<u>447,500</u>	<u>454,000</u>
Total equity and liabilities	<u>6,540,000</u>	<u>2,597,500</u>	<u>990,000</u>

Additional information:

1. Titan Plc acquired 90% of the 950,000 ordinary shares of Iron Ltd for cash of £1,660,000 on 1 January 2014 when the retained earnings of Iron Ltd were £650,000. The fair values of the assets, liabilities and contingent liabilities of Iron Ltd at this date were equal to their carrying amounts, with the exception of a machinery which had a fair value £100,000 in excess of its carrying amount. The machinery had a remaining useful life of 10 years on the date that Titan Plc acquired its shares in Iron Ltd.

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On 1 January 2018, a piece of land of Iron Ltd was valued at £200,000 higher than book value and half of the goodwill was impaired.

2. On 1 January 2018, Titan Plc acquired 60% of the 300,000 ordinary shares of Echo Ltd. The consideration consisted of cash of £40,000 paid on 1 January 2018, ordinary shares of Titan Plc valued at £160,000 and a further cash payment of £110,000, deferred until 1 January 2019. An appropriate discount rate is 10% pa. Only cash consideration has been recorded in the books of Titan Plc.

On 1 January 2018 Echo Ltd's retained earnings were £240,000 and its statement of financial position included goodwill of £36,000 which had arisen on the acquisition of a partnership. In the year ended 31 December 2018 an impairment of £6,000 was recognised by Echo Ltd in relation to this goodwill. The fair values of the other assets, liabilities and contingent liabilities were equal to their carrying amounts.

3. During year 2018 Echo Ltd recorded goods purchased on credit from Iron Ltd for £60,000. At the year end, Echo Ltd held a quarter of these goods in its inventories. Iron Ltd makes all sales at cost plus a mark-up of 25%.
4. Included in the receivables of Titan Plc were £20,000 due from Iron Ltd. Iron Ltd had remitted £10,000 on account of these debts but Titan Plc did not adjust its bank account.

Required:

- a. Prepare the consolidated statement of financial position of Titan Plc as at 31 December 2018.
(21 marks)
- b. With reference to the acquisition of Iron Ltd, and using calculations where appropriate, explain the two methods of calculating goodwill and the non-controlling interest allowed by IFRS 3, *Business Combinations*.
(5 marks)
- c. Explain how the equity section of the consolidated statement of financial position reflects ownership.
(2 marks)
- d. Explain, with reference to the single entity concept, how trading between a parent entity and an associated company is treated in the preparation of consolidated financial statements.
(2 marks)

(Total 30 marks)

End of Paper